

**SEMIANNUAL REPORT TO THE CONGRESS**

**APRIL 1, 2003 – SEPTEMBER 30, 2003**

**OFFICE OF INSPECTOR GENERAL**

**NATIONAL ENDOWMENT FOR THE ARTS**

October 30, 2003

**MEMORANDUM**

TO: Dana Gioia  
Chairman

FROM: Daniel L. Shaw  
Inspector General

SUBJECT: **Semiannual Report to the Congress: April 1, 2003 – September 30, 2003**

The Inspector General Act of 1978 (Public Law 95-452), as amended, calls for the preparation of semiannual reports to the Congress summarizing the activities of my office for the six-month periods ending each March 31 and September 30. I am pleased to enclose the report for the period from April 1, 2003 to September 30, 2003.

The Inspector General's report covers audits, investigations and other reviews conducted by the Office of Inspector General (OIG), and indicates the status of management decisions whether to implement or not to implement recommendations made by the OIG. The President's Council on Integrity and Efficiency developed the reporting formats for Tables I and II to ensure consistent presentation by the Federal agencies. The tables provide only summary totals and do not include a breakdown by auditee.

The Act requires that you transmit the report to the appropriate committees of the Congress within 30 days of receipt, together with any comments you may wish to make. Comments that you might offer should be included in your "Report on Final Action," a management report that is required to be submitted along with the Inspector General's report. We will work closely with your staff to assist in the preparation of the management report. The due date for submission of both reports is November 30, 2003.

I appreciate the continuing support we have received from the Chairman's Office and your managers throughout the Agency. Working together, I believe we have taken positive steps to improve Agency programs and operations. We look forward to continuing these efforts.

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## **NEA PROGRAMS AND OPERATIONS**

Since its founding by the U.S. Congress in 1965, the National Endowment for the Arts (NEA) has offered assistance to a wide range of non-profit organizations and individuals that carry out arts programming. The NEA supports exemplary projects in all the artistic disciplines. Grants are awarded to arts, educational, and community organizations for specific projects rather than for general operating or seasonal support. Most NEA grants must be matched by non-federal sources. During FY 2003, NEA operated on a budget of \$115.7 million and employed a staff of about 150. The President's request for the NEA's FY 2004 budget is \$117.48 million.

## **OIG RESPONSIBILITIES AND RESOURCES**

On October 18, 1988, the President signed Public Law 100-504, the Inspector General Act Amendments of 1988. This law amended the Inspector General Act of 1978, Public Law 95-452, and required the establishment of independent Offices of Inspector General (OIG) at several designated Federal entities and establishments, including the National Endowment for the Arts. The Inspector General is appointed by and serves under the general supervision of the NEA's Chairman. The mission of the OIG is to:

- Conduct and supervise independent and objective audits and investigations relating to NEA programs and operations;
- Promote economy, effectiveness and efficiency within the NEA;
- Prevent and detect fraud, waste and abuse in NEA programs and operations;
- Review and make recommendations regarding existing and proposed legislation and regulations relating to NEA programs and operations; and
- Keep the NEA Chairman and the Congress fully and currently informed of problems in Agency programs and operations.

This semiannual report summarizes the OIG's major activities, initiatives and results for the six-month period ending September 30, 2003. During this period, the OIG consisted of two auditors and one program analyst. (The OIG is authorized one additional auditor position that is not currently filled.) There is no investigator on the staff. In order to provide a reactive investigative capability, we have signed a Memorandum of Understanding with the Inspector General of the General Services Administration (GSA) whereby the GSA's OIG agrees to provide investigative coverage for us on a reimbursable basis as needed. (No investigative coverage from GSA was needed during the recent six-month period.) We have also signed a Memorandum of Understanding with NEA's Office of General Counsel (OGC) that details procedures to be used for providing the OIG with legal services. An OGC staff member has been assigned to provide such services on an as-needed basis.

## **SUMMARY OF WORK COMPLETED BY THE OIG**

During the six-month period ending September 30, 2003, the OIG conducted the following audits, reviews, investigations and other activities.

### **Audits/Reviews**

During the recent semiannual period, the OIG issued 17 review reports. Of those, five reports were based on reviews performed by OIG personnel and 12 reports were the results of OIG desk reviews of audit reports and other materials related to grantee organizations that were required to have audits performed by independent auditors. Overall, our reports contained 17 recommendations, of which five concerned issues of financial management at grantee organizations, two pointed to potential refunds that might be due the NEA, and ten related to systems deficiencies at the NEA.

### **Audit Resolution**

At the beginning of the six-month period, there were no reports awaiting a management decision to allow or disallow questioned costs. During the period, two reports identified \$538,311 in questioned costs and potential refunds totaling \$130,500.

Management decisions were made on one of the reports, to allow \$347,261 in questioned costs and to not seek an \$80,000 refund. At the end of the period, one report remained outstanding with questioned costs of \$191,050 and potential refunds of \$50,500. (See Table I.)

### **Investigations**

The OIG opened one new allegation case during the recent six-month period. This case was closed after a preliminary review, which determined that further investigation was not warranted by the evidence. The one remaining open case is still in abeyance pending the resolution of a related lawsuit. No criminal investigations were performed during the period.

### **Indirect Cost Rate Evaluations**

Indirect costs are incurred for common or joint objectives, which cannot be readily and specifically identified with a particular project or activity. The costs of operating and maintaining facilities, depreciation or use allowances, and administrative salaries and supplies are typical examples of costs that nonprofit organizations usually consider to be indirect.

Indirect cost rates are established by agreement between a non-Federal organization and a Federal agency (usually the agency that furnishes the preponderance of Federal funding) that acts on behalf of all Federal agencies in approving rates with the organization. During this period, the OIG evaluated four indirect cost rate proposals submitted by NEA grantee organizations.

The OIG also makes use of an Indirect Cost Guide, which was issued during the past year. The Guide answers such questions as: What are direct or indirect costs, what is an indirect cost rate, and does an entity need an indirect cost rate? A copy of the Guide can be found on NEA's web site at [www.arts.endow.gov/about/OIG/IndirectCost.html](http://www.arts.endow.gov/about/OIG/IndirectCost.html).

## **Review of Legislation, Rules, Regulations and Other Issuances**

The OIG is required to review and comment on proposed legislation and regulations for their potential impact on the Agency and its operations. During this reporting period, the OIG provided analyses and written commentaries on Agency Administrative Directives, OMB Circulars and other government publications.

## **Technical Assistance**

The OIG provided technical assistance to numerous NEA grantee organizations and their independent auditors. Our efforts included, for example, clarifying and interpreting the audit requirements of OMB Circular A-133, "*Audits of States, Local Governments, and Non-Profit Organizations*," explaining alternative methods of accounting for indirect costs, and advising some of the first-time and smaller organizations on implementing practical accounting systems and internal controls sufficient to assure compliance with their grant agreements.

The OIG also assisted Agency staff with technical issues related to auditing and accounting.

## **Web Site**

The OIG maintains an ongoing Internet presence ([www.arts.endow.gov/about/OIG/Contents.html](http://www.arts.endow.gov/about/OIG/Contents.html)) to assist and inform NEA grantees and Agency employees. The site includes the *Inspectors General Vision Statement*, our two *Financial Management Guides*, our *Indirect Cost Guide*, past *Semiannual Reports to the Congress*, the *OIG Strategic Plan*, information about contacting OIG staff, how to report wrongful acts, information about alternative methods of funding, and answers to frequently asked questions.

## **Other Activities**

During this period, the OIG took part in the activities of the Executive Council on Integrity and Efficiency (ECIE), and allocated resources for responding to requests for information from the Congress and other agencies. We continued to participate in an advisory capacity in the Agency's implementation of the Government Performance and Results Act (GPRA) and the Federal Information Security Management Act (FISMA). The OIG also is working with the Agency's independent auditors as it prepares for the Agency's first financial statement audit, which will be performed for the fiscal year ending September 30, 2003.

## **Strategic Plan & Five-Year Audit Plan**

We have issued our Strategic Plan & Five-Year Audit Plan for the Years 2004 – 2008. The planning methodology that we have adopted is built around the concepts of issues and issue areas. The issue areas are broad categories of prime importance: they highlight the priorities of our customers - Agency management, the Congress and the American people. The individual issues, expressed as questions, represent an assessment of the most significant concerns facing the NEA. The methodology also includes the formulation of annual audit work plans.

## SECTIONS OF REPORT

The following sections of this report discuss the 12 areas specifically required to be included according to Section 5(a) of the Act. Table I shows there were no Inspector General issued reports with questioned costs and Table II also shows that there were no Inspector General issued reports with recommendations that funds be put to better use.

### **SECTION 1 - Significant Problems, Abuses and Deficiencies**

Audits and other reviews conducted by OIG personnel during the current and prior periods have disclosed a few instances of deficient financial management practices in some organizations that received NEA grants. Among these were:

- Reported grant project costs did not agree with the accounting records, i.e., financial status reports were not prepared directly from the general ledger or subsidiary ledgers or from worksheets reconciled to the accounts;
- Personnel costs charged to grant projects were not supported by adequate documentation, i.e., personnel activity reports were not maintained to support allocations of personnel costs to NEA projects;
- The amount allocated to grant projects for common (indirect) costs which benefited all projects and activities of the organization was not supported by adequate documentation; and
- Grantees needed to improve internal controls, such as ensuring a proper separation of duties to safeguard resources and including procedures for comparing actual costs with the budget.

### **SECTION 2 - Recommendations for Corrective Action**

To assist grantees in correcting or avoiding the deficiencies identified in Section 1, the OIG has prepared two "*Financial Management Guides*," one for non-profit organizations and the other for state and local governments. The guides are not offered as complete manuals of procedures; rather, they are intended to provide practical information on what is expected from grantees in terms of fiscal accountability. The guides are available on the NEA's web site.

The guides discuss accountability standards in the areas of financial management, internal controls, audit and reporting. The guides also contain sections on unallowable costs and shortcomings to avoid. In addition, the guides include short lists of useful references and some sample documentation forms.

### **SECTION 3 - Recommendations in Previous Reports on Which Corrective Action Has Not Been Implemented**

There were no significant recommendations in previous reports on which corrective action has not been implemented.

### **SECTION 4 - Matters Referred to Prosecuting Authorities**

No matters were referred to prosecuting authorities during this reporting period.

### **SECTION 5 - Denials of Access to Records**

No denials of access to records occurred during this reporting period.

**SECTION 6 - Listing of Reports Issued**

<b><u>REPORT NUMBER</u></b>	<b><u>TITLE</u></b>	<b><u>DATE OF REPORT</u></b>
<b><u>Oversight Audit Agency Review Reports</u></b>		
OAA-03-03	State of Utah .....	04/23/03
OAA-03-04	State of Maryland.....	05/08/03
OAA-03-05	State of South Carolina.....	05/09/03
OAA-03-06	The John F. Kennedy Center for the Performing Arts and the National Symphony Orchestra .....	06/02/03
OAA-03-07	The John F. Kennedy Center for the Performing Arts and the National Symphony Orchestra .....	06/05/03
OAA-03-08	State of Arizona .....	06/13/03
OAA-03-09	State of Texas.....	06/30/03
OAA-03-10	State of North Carolina .....	07/01/03
OAA-03-11	City of San Antonio, Texas .....	07/01/03
OAA-03-12	State of Oregon.....	07/21/03
OAA-03-13	State of Utah .....	08/13/03
OAA-03-14	State of South Dakota.....	09/02/03
<b><u>Limited Scope Audits</u></b>		
LS-03-01	National Black Touring Circuit, Inc. ....	06/12/03
LS-03-02	New Federal Theatre, Inc. ....	06/12/03
<b><u>Grant Evaluation Reports</u></b>		
GE-03-02	Nikolais/Louis Foundation for Dance, Inc. ....	06/16/03
<b><u>Special Review Reports</u></b>		
R-03-02	Review of NEA's Cooperative Agreements with BHK Arts Consultants, Inc. ....	09/23/03
R-03-03	Fiscal Year 2003 Evaluation of NEA's Compliance with the Federal Information Security Management Act of 2002.....	09/17/03

**TOTAL REPORTS - 17**

**SECTION 7 - Listing of Particularly Significant Reports**

There were no particularly significant reports during the reporting period.

**SECTION 8 - Statistical Tables Showing Total Number of Audit Reports and the Dollar Value of Questioned Costs**

Table I of this report presents the statistical information showing the total number of audit reports and the total dollar value of questioned costs.

**SECTION 9 - Statistical Tables Showing Total Number of Audit Reports and the Dollar Value of Recommendations that Funds be Put to Better Use by Management**

As shown on Table II, there were no audit reports with recommendations that funds be put to better use by management.

**SECTION 10 - Audit Reports Issued Before the Commencement of the Reporting Period for Which No Management Decision Has Been Made by the End of the Reporting Period**

There were no audit reports issued before the commencement of the reporting period for which no management decision has been made by the end of the reporting period.

**SECTION 11 - Significant Revised Management Decisions Made During the Period**

No significant revised management decisions were made during the reporting period.

**SECTION 12 - Significant Management Decisions With Which the Inspector General Disagrees**

There were no significant management decisions that the Inspector General disagreed with during the reporting period.

**TABLE I**

**INSPECTOR GENERAL ISSUED REPORTS WITH QUESTIONED COSTS**

	<u>NUMBER</u>	<u>QUESTIONED COSTS</u>	<u>UNSUPPORTED COSTS</u>	<u>POTENTIAL REFUNDS</u>
A. For which no management decision has been made by the commencement of the reporting period	<u>0</u>	<u>0</u>	<u>(0)</u>	<u>0</u>
B. Which were issued during the reporting period	<u>2</u>	<u>538,311</u>	<u>(538,311)</u>	<u>130,500</u>
Subtotals (A + B)	<u>2</u>	<u>538,311</u>	<u>(538,311)</u>	<u>130,500</u>
C. For which a management decision was made during the reporting period	<u>1</u>	<u>347,261</u>	<u>(347,261)</u>	<u>80,000</u>
(i) Dollar value of disallowed costs	<u>0</u>	<u>0</u>	<u>(0)</u>	<u>0</u>
(ii) Dollar value of costs not disallowed	<u>1</u>	<u>347,261</u>	<u>(347,261)</u>	<u>80,000</u>
D. For which no management decision has been made by the end of the reporting period	<u>1</u>	<u>191,050</u>	<u>(191,050)</u>	<u>50,500</u>
Reports for which no management decision was made within six months of issuance	<u>0</u>	<u>0</u>	<u>(0)</u>	<u>0</u>

**TABLE II**

**INSPECTOR GENERAL ISSUED REPORTS**

**WITH RECOMMENDATIONS THAT FUNDS BE PUT TO BETTER USE**

	<b><u>NUMBER</u></b>	<b><u>DOLLAR VALUE</u></b>
A. For which no management decision has been made by the commencement of the reporting period	0	0
B. Which were issued during the reporting period	0	0
Subtotals (A + B)	0	0
C. For which a management decision was made during the reporting period	0	0
(i) dollar value of recommendations that were agreed to by management	0	0
- based on proposed management action	0	0
- based on proposed legislative action	0	0
(ii) dollar value of recommendations that were not agreed to by management	0	0
D. For which no management decision has been made by the end of the reporting period	0	0
Reports for which no management decision was made within six months of issuance	0	0

**DEFINITIONS OF TERMS USED**

The following definitions apply to terms used in reporting audit statistics:

<b>Questioned Cost</b>	A cost that the Office of Inspector General (OIG) questioned because of alleged violation with a provision of a law, regulation, contract, or other agreement or document governing the expenditure of funds; such cost is not supported by adequate documentation; or the expenditure of funds for the intended purpose is unnecessary or unreasonable.
<b>Unsupported Cost</b>	A cost which the OIG questioned because the cost was not supported by adequate documentation at the time of the audit.
<b>Disallowed Cost</b>	A questioned cost that management has sustained or agreed should not be charged to the NEA grant or cooperative agreement.
<b>Funds Be Put To Better Use</b>	A recommendation made by the OIG that funds could be used more efficiently if management took actions to implement and complete the recommendation.
<b>Management Decision</b>	Management's evaluation of the findings and recommendations contained in the audit report and the issuance of management's final decision, including actions to be taken. Interim decisions and actions are not considered final management decisions for the purpose of the tables in this report.
<b>Final Action</b>	The completion of all actions that management has concluded in its management decision with respect to audit findings and recommendations. If management concluded that no actions were necessary, final action occurs when a management decision was made.

## REPORTING WRONGFUL ACTS

**Anyone, including Agency employees, who learns about or has reason to suspect the occurrence of any unlawful or improper activity related to NEA operations or programs, should contact the OIG immediately. A complaint/referral may be made by visiting the OIG office, calling the OIG at 202-682-5402, emailing at [oig@arts.endow.gov](mailto:oig@arts.endow.gov) or writing to the Office of Inspector General, Room 601, 1100 Pennsylvania Avenue, NW, Washington, DC 20506.**

When contacting the OIG, it will help if you have answers to the following questions:

- Who are the parties involved (names, addresses and phone numbers if possible);
- What is the suspected activity (specific facts of the wrongdoing);
- When and where did the wrongdoing occur;
- How did you learn about the activity (from a third party, actual observation, conclusion drawn from observing or performing different activities, etc.); and
- Where can you be contacted or when will you contact us again.

**The OIG will not disclose the identity of a complainant or informant without consent, unless the Inspector General determines that such disclosure is unavoidable during the course of the investigation. You may remain anonymous, if you choose. Federal employees are protected against reprisal for disclosing information to the Inspector General unless such disclosure was knowingly false.**

